No. 8409

IN THE

United States Circuit Court of Appeals

IN AND FOR THE

NINTH CIRCUIT

J. N. HENDRICKSON,
Complainant,

vs.

EL CAMINO OIL COMPANY, LTD., a corporation,
Respondent.

STATE OF CALIFORNIA,
Creditor and Appellant,

vs.

H. A. MEEK, as Receiver of El Camino Oil Company, Ltd., a corporation,
Receiver and Appellee,

F. R. KENNEY and L. W. WICKES,
Creditors and Appellees.

REPLY BRIEF OF APPELLANT, THE STATE OF CALIFORNIA

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REPLY BRIEF OF APPELLANT, THE STATE OF CALIFORNIA

The appellees, F. R. Kenney and L. W. Wickes have filed a joint appellees' brief herein. These appellees claim to have contract liens upon the

property in the receivership estate herein, prior and paramount to the tax lien of the State of California thereon. It is undisputed that the claim of the State of California in the principal amount of $252,420.29 plus penalties in the amount of $33,-604.91, constitutes a lien upon all of the property of the El Camino Oil Company. (Tr., pp. 84–87.) However, the priority of said tax lien, and the existence and priority of the liens claimed by said individual creditors, are at issue in this appeal. But, regardless of what portion of the claims of said creditors is held to be secured, there will be insufficient assets in this estate to even pay all of the secured claims. Therefore, the real controversy herein is between said individual appellees and the State of California, and the individual creditors being represented by their own counsel, and having filed their separate brief, the interest of the receiver herein, as appellee, is purely academic. Nevertheless, he has seen fit to file an even more extensive brief, as appellee, than was filed by the real parties in interest, the individual creditor appellees. Most of this brief of the receiver presents the same contentions made by said individual creditors in their appellees' brief. Therefore, the State of California will present but a single reply brief, in response to both of said appellees' briefs. For the same reasons, this reply brief will be directed primarily to the arguments presented in the brief of the individual appellees,

Kenney and Wickes, and the references to appellees' brief will, unless otherwise specified, be to the brief of said individual creditors as appellees. In so far as the points made by the receiver are but a repetition of the points made by these appellees, no particular mention will be made of the receiver's brief. However, in so far as the receiver's brief presents any additional points, said points will be specifically answered herein.

THE FACTS

The appellant, the State of California, made a full and correct statement of the facts, in its opening brief, citing the pages of the record on appeal which support said statement. (App. Op. Br., pp. 4–8.) The appellees Kenney and Wickes, the real parties in interest in opposition to the State of California on this appeal, have accepted that statement as "fair and proper," and have therefore not made any additional statement whatsoever. (Br. of Appellees Kenney and Wickes, p. 3.) On the other hand, the appellee H. A. Meek, as receiver, notwithstanding he has no real interest whatsoever in the present controversy between the adverse lien claimants, has raised a question as to the accuracy of the statement of the appellant that the $10,000 note and chattel mortgage securing the same were executed on June 6, 1930, and that the $80,000 note and the deed of trust securing the same were executed on June 7, 1930. (Br. of Appellee Meek, pp. 4–5.)

The stipulation of facts shows that the $10,000 note and the chattel mortgage to secure the same were both executed on June 6, 1930. (Tr., pp. 22, 24, 26.) The same stipulation shows that the trust deed, purportedly securing the $80,000 note, was executed on June 7, 1930 (Tr. pp. 28, 38). Said trust deed recites that it was executed for the purpose of securing an $80,000 note "of even date herewith". (Tr., p. 30.)

Furthermore, extensive briefs were filed with the trial court upon the basis of the facts being as thus recited, and, pursuant to those briefs and the stipulations on file, said court, in its opinion, recited that on June 6, 1930, the El Camino Oil Company executed one promissory note to said Kenney and Wickes for $10,000, secured by chattel mortgage upon certain of its equipment, and on June 7, 1930, another promissory note for $80,000 secured by a trust deed upon certain real property. (Tr., pp. 75-76.) This opinion was, by the order of the court, incorporated as the findings of fact and conclusions of law of said court. (Tr., p. 87.)

Thus, the record herein squarely supports the statement of facts made by the appellant, and the belated attempt of the Receiver to cast doubt upon these facts is of no avail. In any event, it is not necessary to go further into this question of fact because of certain concessions which the appellant will make hereinbelow.

POINT I

"NO PART OF THE CLAIM OF F. R. KENNEY AND L. W. WICKES IS SECURED BY THE CHATTEL MORTGAGE OF JUNE 6, 1930"

As its first point, the appellant urged the foregoing proposition, upon the ground that the $10,000 note of June 6, 1930, which was secured by the chattel mortgage of even date, was fully satisfied, and the mortgage discharged, by the accounting had between the parties to said instruments subsequent to their execution, whereby the amount of the indebtedness of the El Camino Oil Company to said individual creditors was ascertained to have been $78,046.60, only, or, in other words, in an amount less than that of the note of June 7, 1930, purportedly the deed of trust of even date. Appellant now concedes, however, that, while the record upon this appeal discloses that the $10,000 note was of earlier date than the $80,000 note, said record does *not* disclose that the $10,000 note was of earlier *date of maturity* than the $80,000 note. For this reason, the provisions of subdivision 3 of section 1479 of the California Civil Code, set forth in appellant's opening brief, (pp. 16-17) are inapplicable.

Star Mill & Lumber Co. vs. *Porter,* 4 Cal. App. 470, 473 (1906).

While it appears from the last cited case that, under such circumstances the credit to which the debtor is entitled should be applied proportionately

amongst his several obligations, the appellant herein does not wish to press this point, inasmuch as, even if the credit in question were so applied, this would still leave an unpaid balance on said $10,000 note in excess of the value of the security afforded by said chattel mortgage. The right to such an application would therefore be of academic interest only. The appellant therefore withdraws the first point urged in its opening brief. For this reason, the other arguments presented by the respective appellees upon this first point will not be further considered herein. So far as the lien of said chattel mortgage is concerned, the appellant is content to rely upon the proposition discussed hereinbelow, that, in any event, the *entire* tax lien of the State of California is paramount to *any* contract lien which the individual claimants may have.

POINT II

THE DEED OF TRUST EXECUTED JUNE 7, 1930, BY THE EL CAMINO OIL COMPANY DID NOT CREATE AND DOES NOT CONSTITUTE A VALID AND EXISTING LIEN AS AGAINST THE STATE OF CALIFORNIA UPON THE PROPERTY DESCRIBED IN SAID DEED OF TRUST AS PARCEL II

In answering the argument of the appellant in support of the second proposition stated in its opening brief, the appellees Kenney and Wickes assert that "The flaws in appellant's argument lie in its assumptions first, that a leasehold is personal property, and second, that a conveyance in trust to

secure payment of an obligation is a chattel mortgage." (Appellees' Br., p. 9.)

A. A LEASEHOLD INTEREST IS PERSONAL PROPERTY

In support of its contention that a leasehold interest is real property, said appellees first quote section 657 of the California Civil Code which defines property as being either "1—real or immovable; or, 2—personal or movable." Said appellees then cite certain Federal Court cases to the effect that a leasehold is a chattel real and immovable. (Appellees' Br., pp. 9-10.) From this they conclude that a leasehold interest is "therefore real property by definition in California." (Appellees' Br., p. 10.) A reading of said cases discloses that there is nothing therein favorable to the contention of said appellees. On the contrary, they show that a leasehold interest is *personal property.*

However, assuming for the purpose of argument that the Federal cases cited hold that a leasehold is a chattel real and immovable, it is submitted that this cannot justify the appellees' conclusion that *in California* a leasehold interest is *real property.* The appellees concede that at common law, leasehold estates were personal property (Appellees' Br., p. 10), but contend that by reason of the provisions of said section 657 of the California Civil Code, the Legislature has clearly expressed its intention that a leasehold interest is real property. Said section 657 was intended to be a general classi-

fication, merely, and not a full and complete definition. This is demonstrated by the further definitions of different kinds of real property, as contained in sections 658 to 662 of the California Civil Code, set forth in the brief of the Appellee Meek (pp. 11-12). *None* of the definitions in said sections embrace a *leasehold interest.* And section 663, which concludes these definitions of different classes of property defines *personal property* as being "every kind of property that is not real."

In any event, of course, the California courts are the final authority upon this question as to whether a leasehold interest is real property or personal property. And even the appellees Kenney and Wickes, the real parties in interest in this appeal, concede (Appellees' Br., p. 10) that "the California courts have in several instances dealt with leasehold estates as though the same were personal property," (See cases cited in Appellant's Opening Brief, page 21.)

The receiver, however, contends that the courts of California have *not* consistently held a mere leasehold interest in land to be either real property or personal property, citing *S. P., L. A. & S. L. R. Co.* vs. *City of Los Angeles,* 180 Cal. 18 (1919) (Br. of Appellee Meek, p. 13). That case refers solely to the question of what is real property, within the meaning of California Political Code section 3617, *for purposes of taxation.* It is well settled that *for tax purposes* a leasehold interest is real property.

See *Jameson Petroleum Co.* vs. *State,* 11 Cal. App. (2d) 677 (1936), and the cases therein cited. However, even these tax cases recognize that the rule therein applied is merely an *exception* to the general rule that a leasehold estate is *personal* property. (Ibid.) It is firmly established in California that the common law definition of leasehold estates as *personal property* applies in this State in the absence of a particular statutory provision which is controlling.

Dabney vs. *Edwards,* 5 Cal. (2d) 1, 6-7 (1935), and cases cited;
Guy vs. *Brennan,* 60 Cal. App. 452, 454-455 (1923); and
Jeffers vs. *Easton, Eldridge Co.,* 113 Cal. 345 (1896).

The California cases upon this point are so clear that a minute analysis thereof would be presumptious. Appellant therefore made no error in "assuming" that a leasehold interest in California is personal property. Such is the *law* in California.

The receiver further suggests that whether or not the leasehold interest was personal property, the trust deed covers, in addition to said leasehold interest, certain fixtures, which he claims are unquestionably real property, and so the trust deed is valid as to that portion of Parcel II. (Br. of Appellee Meek, pp. 14-17.) It is worthy of note that the individual lien claimants themselves have not deemed such a contention meritorious. However,

since the receiver has raised the issue with apparent seriousness it must be answered.

The portions of the trust deed which are pertinent upon this point are as follows:

> "Trustor hereby GRANTS to TRUSTEE, IN TRUST, WITH POWER OF SALE, all that property in the City of Los Angeles County, of Los Angeles, State of California, described as:
>
> PARCEL I: Lot Nine (9), Block F, Tract 6482, as per Book 86, Pages 72-73 of Maps, Records of Los Angeles County, State of California;
>
> and also Trustor hereby grants, conveys, transfers, assigns and sets over to Trustee, in trust, with power of sale, all that property in the County of Los Angeles, State of California, described as:
>
> All Trustor's right, title and interest, as Lessee, in and to that certain written lease dated September 16, 1929, between Matilda E. Richer, Lessor, and El Camino Oil Company, a corporation, Lessee, pertaining to and covering
>
> PARCEL II: The West Five (5) acres of the North Fourteen (14) acres of the East Fifty-five (55) acres of the South Half (S $\frac{1}{2}$) of the Northwest quarter (NW$\frac{1}{4}$) of Section 8, Township 3 South, Range 11 West, San Bernardino Base and Meridian.
>
> which said lease was recorded on the 24th day of September, 1929, in Book 9300, page 229 of Official Records in the office of the County

Recorder of Los Angeles County, State of California, including Trustor's right under said lease to purchase said premises upon the terms and conditions set forth in said lease.

Said grant, transfer, and assignment of said Trustor's interest, as Lessee, in and to said lease is hereby made to said Trustee upon the express understanding and agreement between Trustor and Trustee that Trustee is not to be liable upon any of the covenants, obligations and requirements of said lease.

It is expressly understood and agreed that all that certain oil refinery located upon Parcel II above described and all that certain bulk plant located upon Parcel I above described, including all machinery, equipment and fixtures and all tanks, vats, pumps, boilers, engines, meters, pipes, stills, and fractionating towers now situated upon the above described premises, or either of them, in whatever manner affixed or attached to either of said parcels of real property, are and shall be deemed to be real property and expressly included in the above grant, transfer and assignment." (Tr., pp. 28-30.)

The real property described in Parcel II was vacant and unimproved at the time when it was leased to the El Camino Oil Company, Ltd. (Tr., p. 44.) It was leased for the purpose of erecting, maintaining and operating an oil refinery, absorption plant and cracking plant (Tr., p. 52), and said oil company accordingly erected such a refinery plant and equipment thereon. (Tr., pp. 44–45.) Under said lease, it was expressly provided that

all equipment and fixtures and all personal property erected on the leased premises by the lessee "may be removed by the lessee at the termination of this lease, or any extension thereof, even though the same may be attached to said premises," subject to certain conditions not here material. (Tr., p. 54.)

It is not necessary at this time to enter into any controversy as to what portion of said equipment was personal property and what portion fixtures, as between the lessor and the lessee. In so far as said equipment and structures were *personal property,* the trust deed was clearly invalid, for the reason that it was not executed as required for encumbrances of personal property not accompanied by a transfer of possession. And in so far as the property might otherwise have been real property, the only interest which the lessee could claim therein, and therefore the only interest therein which said lessee could, as trustor, encumber, was such rights as it had, *under the lease,* to remove said property. Such an interest, like the lease itself, is personal property, and any encumbrance thereof must be made in the manner required for personal property.

Thus, in *Summerville* vs. *Stockton Milling Co.,* 142 Cal. 529 (1904) it was held that a judgment, which constituted a lien upon all *real* property of the judgment debtor, did *not* constitute a lien upon the judgment debtor's right, *as lessee,* to certain

crops upon the land of which he was lessee. In other words, the leasehold interest, *and the lessee's right thereunder to the crops,* were *personal property.* This case has been repeatedly cited with approval by the California Supreme Court, and as recently as December, 1935, in *Dabney* vs. *Edwards,* 5 Cal. (2d) 7.

See also

Summerville vs. *Kelliher,* 144 Cal. 156 (1904); and

Belieu vs. *Power,* 54 Cal. App. 244 (1921), hearing by Supreme Court denied.

And in *Barnum* vs. *Cochrane,* 143 Cal. 642, (1904) the California Supreme Court held that a sale of hotel property situated on leased premises, *with the privilege of removal of the improvements* upon compliance with the lease, *is a sale of personal property.*

The receiver claims that the case of *Commercial Bank* vs. *Pritchard,* 126 Cal. 600 (1899), definitely determines that the improvements placed on the real property by the lessee were real property, in so far as said improvements constituted fixtures. (Br. of Appellee Meek, pp. 16–17.) In that case, the lessee of certain property, who had the right to remove, at the end of the term, a warehouse he had erected on the leased property, mortgaged said warehouse and also made an assignment of his lease to the mortgagee. "The mortgage was verified by the mortgagor and mortgagee *as a mort-*

gage of personal property, and was properly acknowledged'' (126 Cal. 601; emphasis added), and was recorded as a chattel mortgage (126 Cal. 602). Thereafter, the lessee *sold* said warehouse to a third person. The mortgagee brought *action to foreclose his mortgage,* and judgment in the trial court was in favor of the purchaser of the warehouse, as against said mortgagee. On appeal, the judgment was reversed. Thus, the *decision,* was merely that a *duly executed* assignment and mortgage of a leasehold estate, impressed a lien upon the entire leasehold interest of the lessee, including his right to the improvements. Therefore, the case is really favorable to the appellant upon this proposition, and is entirely in accord with *Summerville* vs. *Stockton Milling Co., Summerville* vs. *Kelliher,* and *Barnum* vs. *Cochrane, supra.* In so far as any of the language in the opinion of the commissioners who wrote the opinion in the case relied upon by the receiver, may appear to hold that a leasehold estate, including any right thereunder to improvements, is *real property,* the opinion has been definitely disapproved by not only the concurring opinion of Mr. Justice McFarland, in that case, (126 Cal. 606) but by subsequent decisions in which said case is cited or considered. Thus, in *Guy* vs. *Brennan,* 60 Cal. App. 452 (1923), after holding that the sale of a leasehold interest was the sale of personal property rather than real property, the court said, at pages 456–457:

"There is nothing in *Commercial Bank* v. *Pritchard,* 126 Cal. 600 (59 Pac. 130) which conflicts with the foregoing views. That case, following the reasoning in *Garber* v. *Gianella,* 98 Cal. 527 (33 Pac. 458), holds that an instrument whereby a lease is *created* (emphasis added) must be deemed to be a 'conveyance' for all the purposes mentioned in sections 1213 and 1214 of the Civil Code. The court was obliged so to hold because, by section 1215 of the Civil Code, there is an express legislative declaration that the term 'conveyance,' *as used in sections 1213 and 1214,* shall embrace every *instrument,* except wills, whereby *any* estate or interest in real property is created, aliened, mortgaged or encumbered. But because the legislature has said, in effect, that, for the purposes of the law respecting the recordation of conveyances, a written instrument whereby a leasehold interest is *created* (emphasis added) shall be deemed to be a 'conveyance,' *it does not necessarily follow that the leasehold interest conveyed by such instrument is 'real estate.'* (Emphasis added.)

The words 'real property,' as defined by section 14 of the Civil Code, subdivision 3, are 'coextensive with lands, tenements and hereditaments.' The learned author of the majority opinion in *Commercial Bank* v. *Pritchard, supra,* seems to have used the terms 'real estate' and 'real property' interchangeably. It doubtless was in view of this laxity in the commissioner's use of two expressions which, technically, are not convertible terms, that Mr. Justice McFar-

land was prompted to write a separate but concurring opinion so as to avoid any possible future misconception as to the real purport and extent of the court's decision. That this was the purpose of the concurring opinion seems evident from its language, Mr. Justice McFarland saying: 'I concur in the judgment; but the opinion of the commissioner *might, perhaps* (italics ours), be construed as holding, generally, that an estate for years in land is real property, which, of course, is not so. An estate for years is, in its nature, personal property—a chattel real; and it is subject for most purposes to the law which applies to personal property. (See *Jeffers* v. *Easton,* 113 Cal. 345, where the subject is discussed and our code division of property into real and personal is shown to be, substantially, that of the common law.)'" (Emphasis by the court, except where stated to have been added.)

This latter case has also been approved by the California Supreme Court as recently as December, 1935, in said case of *Dabney* vs. *Edwards, supra,* at pp. 7–8.

It is therefore submitted that the only interest which the El Camino Oil Company in and to Parcel II in said deed of trust was and is personal property under the law of the State of California.

B. A TRANSFER OR ENCUMBRANCE OF PERSONAL PROPERTY, IN ORDER TO BE VALID AS TO CREDITORS OF THE TRANSFEROR OR ENCUMBRANCER, MUST BE ACCOMPANIED BY A

TRANSFER OF POSSESSION OR BE MADE IN THE MANNER REQUIRED FOR A CHATTEL MORTGAGE

The appellees Kenney and Wicks contend that the appellant's argument in support of its second proposition stated in the appellant's opening brief is unsound for the further reason that it assumes "that a conveyance in trust to secure payment of an obligation is a chattel mortgage." (Appellees' Br., p. 9.) Appellant submits that this is an erroneous statement. Appellant does not contend, nor is it necessary that it assume, that a conveyance in trust to secure payment of an obligation *is* a chattel mortgage. Appellant merely contends that section 3440 of the California Civil Code requires *all* transfers of personal property to be accompanied by a change of possession or to be made in the manner required for the execution of mortgages as provided by law, that is, as provided in section 2957 of the California Civil Code.

Said appellees quote section 2924 of the California Civil Code defining a mortgage. This definition excludes a transfer in trust. From this the appellees conclude that "by this express exclusion of transfers in trust from the definition of mortgages it follows that a conveyance in trust is not a mortgage, and that the rules applicable to the valid execution of mortgages, chattel or otherwise, have no application to deeds of trust." (Appellees' Br., p. 10.) However, the appellant is not relying upon the definition or nature of a chattel mortgage as

being the basis for its contention that the encumbrance here in question must be executed as a chattel mortgage in order to be valid as against the State of California. The appellant is relying upon the provisions of section 3440 of the Civil Code as requiring the transfer to be *executed as required for a chattel mortgage,* regardless of what the nature of the encumbrance may be.

In other words, under said section 3440, there are only two ways of making a transfer or encumbrance of personal property, which will be valid as against those who are the creditors of the transferor or encumbrancer. One is to accompany said transfer by an immediate delivery followed by an actual and continued change of possession of the thing transferred. The other is to make the transfer by way of a mortgage when allowed by law. Manifestly, such a mortgage, being of personal property, must be executed in the manner provided by section 2957 of the Civil Code. The encumbrance here in question was not so executed, nor was there any change of possession. Therefore, by the express provisions of said section 3440 said encumbrance is void as against the State of California.

Said appellees further attempt to avoid this conclusion by claiming that in any event they do not hold a mere lien upon the property of their debtor, but that, under their trust deed, they hold legal title. (Appellees Br., pp. 10-11.) Assuming for the purpose of argument that this is entirely true, it

does not clearly appear just how this is advantageous to the appellees. Section 3440 of the Civil Code applies to the transfer of the legal title as well as to mere encumbrances, and there was no transfer of possession as required by that section. However, even if this were not so, the statement of the appellees that the "California courts recognize the legal distinction between deeds of trust and mortgages, and hold that even though the practical effect of a deed of trust is similar to that of a mortgage containing a power of sale, nevertheless a deed of trust is not a mortgage and it is legally impossible to hold that the trustee has a lien on the property conveyed in trust, or to hold that the property is subject to a lien" (Appellees' Br., p. 11) is not true under circumstances such as are involved herein. The California cases cited following this statement in Appellees' Brief (page 11), do contain language to the effect stated by the appellees. However, when the courts of California are squarely confronted with the question of the priority of liens, said courts uniformly hold that a deed of trust *is a lien,* and, as such, subject to the general rules for determining the priority of liens.

Miller vs. *Citizens Tr. & Savings Bank,* 128 Cal. App. 295 (1932);

Wasco Creamery etc. Co. vs. *Coffee,* 117 Cal. App. 298, (1931; hearing by Supreme Court denied)

And see *San Mateo County Bank* vs. *Dupret,* 124 Cal. App. 395 (1932).

Said appellees further assert that "trusts in personalty are valid in California." (Appellee's Br., p. 11.) The appellant does not deny this. However, it should be noted that in the cases cited by the appellees in this regard there was a sufficient *transfer of possession of the res* to satisfy section 3440 of the California Civil Code. Appellant concedes that *if* said section 3440 is complied with, there may be a trust of personal property which is valid even as against other creditors of the trustor, the same as there may be a transfer of the full title to personal property, which is valid as against other creditors of the transferor *if* said section is complied with. But *no* transfer or encumbrance of personal property, by whatever legal device this is attempted, is valid as against other creditors of the transferor or encumbrancer unless there is either a transfer of possession or an encumbrance executed and recorded as required by law for a *mortgage* of personal property. In the present case there was neither. Therefore, the attempted encumbrance of the El Camino Oil Company's leasehold interest described as Parcel II in said deed of trust is void as against the State of California.

The receiver has not added any substantial argument to that presented by the other appellees and answered hereinabove. In particular it should be noted that *neither* of the appellees make any effort to answer the case of *Farmers State Bank* vs. *Schell,* 214 Pac. 825 (Wash. 1923) which squarely

holds in accordance with the contention of the appellant herein.

The District Court erred in holding that the trust deed here in question created and constitutes a valid and existing lien as against the State of California, as to Parcel II described in said trust deed. Said Parcel II, being solely the interest of the El Camino Oil Company under its *lease,* is *personal property.* As personal property, *any transfer* or encumbrance thereof is subject to the provisions of section 3440 of the California Civil Code: to be valid as against other creditors, the transfer or encumbrance must be accompanied by a change of possession, or must be executed as required for a chattel mortgage. In the present case neither of these requirements was fulfilled. The order of the District Court should be modified accordingly.

POINT III

THE DISTRICT COURT ERRED IN ORDERING THAT SAID CLAIM OF F. R. KENNEY AND L. W. WICKES CONSTITUTES A LIEN UPON THE PROPERTY DESCRIBED IN SAID CHATTEL MORTGAGE AND DEED OF TRUST, PRIOR AND PARAMOUNT TO THE LIEN OF THE STATE OF CALIFORNIA UPON SAID PROPERTY, FOR PENALTIES ADDED TO LICENSE TAXES DUE ON ACCOUNT OF MOTOR VEHICLE FUEL SOLD AND DELIVERED BY THE EL CAMINO OIL COMPANY, LTD., FROM AND INCLUDING THE 1st DAY OF APRIL, 1930, TO AND INCLUDING THE 10th DAY OF JUNE, 1930

In reply to this third proposition of the appel-

lant, the appellees Kenney and Wickes assert that the statement of the appellant that since the penalty, when and if it arises, becomes a part of the tax, the lien for the penalty must date back to the time of the accrual of the tax "is not well taken in law or logic. It is not logical for the reason that there are open alternatives and the arbitrary choice of the alternative favorable to the appellant is wish-thinking, not reason." (Appellee's Brief, pp. 12-13.)

In its opening brief the appellant pointed out that this court has ruled that the penalty which is provided for by the tax statute here involved, is a part of the tax, and, as such, is a lien upon the property of the tax debtor in the hands of the receiver.

State of California vs. *Hisey,* 84 Fed. (2d) 802, 805; and cases cited, especially,
Appeal of City of Titusville, 108 Pa. 600; and *Northern Finance Co.* vs. *Byrnes,* 5 Fed. (2d) 11, at 12 (8 C.C.A.1925).

Furthermore, as was pointed out in appellant's brief herein, the tax statute in question specifically provides that "said tax shall be a lien upon all of the property of the distributor. It shall attach at the time of the delivery or distribution subject to the tax * * * " and if said tax is not paid prior to the delinquency date specified in said section "ten per cent penalty shall be added thereto for delinquency." (Section 4 of Calif. Stats. of 1923, p. 572, as amended by Calif. Stats. 1925, p. 659.)

From the foregoing decisions and from the statute itself the appellant, by the process that the appellees choose to designate as "wish-thinking," reached the conclusion that the lien for the penalties necessarily attached at the time specified in the statute, namely, at the time of the delivery or distribution subject to the tax. If this be wish-thinking, then the appellant trusts that this honorable court will be "guilty" of the same thinking process.

Said appellees state that "It is just as logical, and more natural, to maintain that the lien for the penalty attaches at the time the penalty comes into existence, as to maintain the lien dates back." (Appellees' brief, page 13.) Said appellees entirely overlook, however, the specific provision of the statute that the lien shall attach "at the time of the delivery or distribution, subject to the tax." In the language of this court in *State of California* vs. *Hisey, supra,* "If the penalty, as well as the tax, is a lien upon the property in the hands of a receiver, as the statutes of California provide, it is difficult to see how the payment of the penalty can be differentiated from the payment of the lien for the tax."

The case of *W. P. Fuller & Co.* vs. *McClure,* 48 Cal. App. 185, cited by said appellees (Appellees' brief, page 13) is not at all in point, nor does it relate to a situation which is even analogous to that which is involved herein. The California cases

cited by the appellant (Appellant's Op. Br., p. 28) clearly demonstrate the theory upon which tax liens are related back to the date as of which the statute prescribes the lien shall attach. If the penalty, as a part of the tax, is a lien the same as the tax, then there would appear to be no reason why this same doctrine should not apply with regard to the lien for said penalties.

The receiver, as appellee, in addition to presenting substantially the same contention (Brief of Appellee Meek, pp. 25–26), again conceives it as his duty to present in addition thereto, the further propositions that, (1) the state *does not even have a lien* for its penalty, (Brief of Appellee Meek, pp. 23–25) and that (2) in any event, it was purely within the discretion of the District Court to entirely *disallow* the appellant's claim for penalties. (Brief of Appellee Meek, p. 26.) Even the District Court below has decided adversely to these contentions of the receiver. Said court squarely held that the claim of the State of California including the penalty, *is a valid and existing claim* against the receivership estate, *and a lien* upon all of the property of the El Camino Oil Company, Ltd. (Tr., p. 84.) Thus, if, as said appellee contends, it is within the *discretion* of the District Court to allow or disallow the claim for penalties, said court has exercised its discretion in favor of the appellant. Furthermore, this proposition of said appellee, is utterly unsound, and squarely con-

trary to the decision of this court in *State of California* vs. *Hisey, supra.*

As to said appellee's contention that the penalties do not constitute a *lien* under the provisions of section 4 of the tax act here in question, it is submitted that said *Hisey* case again is squarely contrary to the position taken by the receiver herein. Said receiver, however, points to the amendment of said section 4, in 1931, providing for the enforcement of the lien of the tax by seizure and sale of certain property of the tax debtor by the State Controller. (Section 4 of Calif. Stats, 1931, pp. 105, 1652, 2001 and 2288, as cited in brief of Appellee Meek, pp. 24–25.) The appellant is pleased that said appellee has chosen to call this amendment to the attention of this court. For the amendment does not, as said appellee contends, show that the lien which had theretofore existed, did not include the penalties which were added to the amount of the tax. On the contrary, said 1931 amendment clearly shows that the tax lien had always included the entire amount of the tax indebtedness including the penalties added thereto by reason of delinquency.

Prior to said 1931 amendment, the only method for enforcing the lien which was created by section 4 of the tax statutes was by an action in a court of equity to enforce said lien. (See *State of California* vs. *Hisey,* 84 Fed. (2d) 802, at 804.) Manifestly, the Legislature deemed that this method of

enforcing the lien was entirely inadequate. Therefore, in 1931, without in any degree or in any particular changing the *lien,* the Legislature added certain provisions to section 4 for the *enforcement* of said lien by seizure of the property by the State Controller. The portion of section 4 of the tax act quoted by the appellee Meek at page 24 of his brief, (i.e., the amendment of 1931) does not *create* a lien for the penalties. It *assumes the existence* of such a lien and merely provides an additional method of enforcing the lien which already existed under the statute.

Thus, even if the question were a new one and had not previously been ruled upon by this court, it would follow as a matter of principle that the penalties which were added to the amount of the tax upon delinquency, became a part of said tax and were secured by the same lien which secured the principal of the tax. The District Court herein has so ruled. Said District Court therefore erred in making its order that the lien for penalties which were added to the taxes which had accrued prior to the recording of the mortgage and trust deed of the appellees Kenney and Wickes did not attach as of the same date that the lien for said taxes attached, namely, at the time of the delivery or distribution subject to the tax.

POINT IV

SAID DISTRICT COURT ERRED IN ORDERING THAT THE CLAIM OF F. R. KENNEY AND L. W. WICKES

CONSTITUTES A LIEN UPON THE PROPERTY DESCRIBED IN SAID DEED OF TRUST AND CHATTEL MORTGAGE PRIOR AND PARAMOUNT TO THE LIEN OF THE STATE OF CALIFORNIA UPON SAID PROPERTY FOR LICENSE TAXES DUE ON ACCOUNT OF MOTOR VEHICLE FUEL SOLD AND DELIVERED BY SAID EL CAMINO OIL CO., LTD., SUBSEQUENT TO THE 10th DAY OF JUNE, 1930, TOGETHER WITH PENALTIES THEREON FOR DELINQUENCY

In regard to this fourth proposition of the appellant, neither of the appellees dispute the *power* of the Legislature to make a tax lien paramount to an antecedent contract lien. Each of said appellees, however, contends that the Legislature of the State of California has not, in the tax law here in question, exercised this power. The question is thus solely one of statutory construction.

The appellees Kenney and Wickes have divided the provisions of the statute relating to the effect of the tax lien into two parts. They state that the statute, after creating the tax lien, provides, first, that the lien shall have the effect of an execution duly levied against all property of the distributor, and, secondly, that said lien shall remain until the tax is paid or the property sold for the payment thereof. Referring to the first of these provisions the appellees argue that since execution liens do not have priority over antecedent contract liens, the legislative intention is thereby made apparent that the tax liens should not take priority over

valid liens prior in time. (Appellees' brief, pp. 14–16.) Appellant does not rely on this portion of the statute as having the effect of making the tax lien paramount to antecedent contract liens, so the argument of the appellees based thereon need not be answered.

Referring to the second portion of the statutory provisions relating to the effect of the lien, the appellees Kenney and Wickes state that "it is clear that such language was added in order to remove a possible bar to enforcement of the tax lien after a period of five years." (Appellees' brief, p. 16.) In other words, they contend (as the appellant contended in the case of *Sunset Oil Company* vs. *State of California,* No. 8182 before this court, decided January 18, 1937), that the statutory provision that the tax lien shall remain until the tax is paid or the property sold for the payment thereof relates solely to the *duration* of the lien rather than to its *dignity.*

Conceding, for the purpose of argument, that *one* effect of said provision may be to remove a possible bar to enforcement of the tax lien after a period of five years, it does not necessarily follow that this is the *only* effect of said provision. Nor do the appellees present any sound reason for such a conclusion. Rather, they merely *assume* this conclusion. There is nothing in the statute or in reason which justifies such an assumption.

Furthermore, this assumption merely evades the

question. Clearly, if a lien is of the "duration" which is provided for the tax lien in question, it is of paramount "dignity" to any other lien which may exist upon the property. Otherwise it could not *be* of the prescribed "duration." As was pointed out in appellant's opening brief, it is not apparent how it would be possible for the tax lien to remain until the tax is paid or the property sold for the payment thereof, if the tax lien is inferior to antecedent contract liens the enforcement of which might wipe out the tax lien. A tax lien can not bind property until the tax is paid, if, without the tax being paid at all, it can be wiped out by the foreclosure of an earlier dated mortgage or trust deed.

The appellees place great reliance upon the case of *Guinn* vs. *McReynolds* (1918) 177 Cal. 230, 170 Pac. 421, as supporting their contention that it does not appear by reasonable inference from the provisions of the Motor Vehicle Fuel License Tax Act that the Legislature intended that the tax lien created by said act should be paramount to antecedent contract liens. It is true that said case holds that a certain tax lien there in question was not paramount to an earlier dated mortgage lien. The court said, "We find nothing in section 2322a of the Political Code which can be said to indicate an intent to make the county's lien superior to other liens earlier in time." That section provided for the eradication, by the county horticultural commissioner, of infectious pests, and at the time involved in said case, contained the following pro-

visions, only, in regard to the existence and status of a lien for the charges there in question:

> "The expense thereof shall be a county charge, and the board of supervisors shall allow and pay the same out of the general fund of the county. Any and all sum or sums so paid shall be and become a lien on the property and premises from which said nuisance has been removed or abated in pursuance of this chapter. A notice of such lien shall be filed and recorded in the office of the county in which the said property and premises are situated, within thirty days after the right to the said lien has accrued. An action to foreclose such lien shall be commenced within ninety days after the filing and recording of said notice of lien, which action shall be brought in the proper court by the district attorney of the county in the name and for the benefit of the county making such payment or payments, and when the property is sold, enough of the proceeds shall be paid into the county treasury of such county to satisfy the lien and costs; and the overplus, if any there be, shall be paid to the owner of the property, if he be known, and if not, into the court for his use when ascertained."

In the principal case, on the other hand, when the State's tax lien accrued the tax statute specifically provided that the lien for the taxes here in question "shall remain until the tax is paid or the property sold for the payment thereof." Clearly, the decision in the cited case can not control here, in view of the very evident differences between the

statutory provisions relating to liens in the respective cases. The cited case does not even purport to construe the effect of such a statutory lien as is involved in the principal case.

The appellees seek to distinguish the case of *California Loan & Trust Co.* vs. *Weiss* (1897), 118 Cal. 489, 50 Pac. 697, upon the ground that the language of the decision with respect to the provisions of section 3716 of the California Political Code, providing that the lien for personal property taxes shall remain until the tax is paid or the property sold for the payment thereof, "is mere dicta, and it is submitted that, in the light of the great weight of authority to the contrary, further weight should not be given to this unguarded dicta." (Appellees' Br., p. 18.) However, one of the decisions which the appellees cite as constituting the "great weight of authority," clearly demonstrates that other *courts* do *not* consider that the language of the California Supreme Court in said *Weiss* case as merely "unguarded dicta."

See

Scottish American Mortgage Co. vs. *Minidoka County* (Idaho, 1928), 272 Pac. 498, 501.

In that case the Idaho court *expressly rejected* the interpretation of the California Supreme Court, not as "unguarded dicta," but as being an *erroneous decision.* However, the decision in the *Weiss* case is the law in California, and was the law for a period long prior to the time when the Legislature

borrowed the same language which was used in said section 3716, for use in the lien provisions of the Motor Vehicle Fuel License Tax Act. Under the circumstances it certainly can not be assumed that the California Legislature intended to use said language in any other sense than that in which it was construed by the California Supreme Court.

The decisions in other states manifestly can not be of any bearing upon the question of the proper construction to be placed upon the language in question, *when used by the California Legislature after the decision in the Weiss case.* However, lest it be assumed that the appellant concedes that the "great weight of authority" is opposed to the decision reached in California, this court's attention is invited to the following cases which are in accord with the decision reached in this State:

Eaton's Appeal, 83 Pa. State 152;
Union Central Life Insurance Co. vs. *Black,* 247 Pac. 486 (Utah, 1926);
New York Terminal Co. vs. *Gaus,* 98 N. E. 11 (N. Y., 1912);
In re Century Steel Co. of America, 17 Fed. (2d) 78 (2d C. C. A., 1927);
Seaboard National Bank vs. *Rogers Milk Products Co., Inc.,* 21 Fed. (2d) 414, 418 (2d C. C. A., 1927).

Thus, it appears that, to say the least, the view of the California Supreme Court upon the question is not singular.

Finally, this court has already held in the recent case of *Sunset Oil Company* vs. *State of California* (No. 8182, decided January 18, 1937), that the lien of taxes such as those here in question is paramount to antecedent contract liens. At the time the appellant's opening brief was filed herein, the cited case had been decided, but the opinion therein omitted any reference to the question of the priority of the tax lien, notwithstanding that question was necessarily decided in said case. This was pointed out in the appellant's opening brief herein (p. 37). Thereafter, on February 15, 1937, this court, on its own motion, made an order amending the opinion theretofore filed therein, by the addition of the following paragraph immediately preceding the closing paragraph of the opinion:

> "The appellant purchased all the property of the Sunset Pacific Oil Company at foreclosure, held Dec. 14, 1934. The sale was confirmed Dec. 29, 1934. The mortgage foreclosed antedated the lien for the gasoline tax in dispute. The purchaser claims that the mortgage lien is superior to the tax lien, and hence that the sale of the property extinguished the tax lien. The gasoline tax law of the State of California provided that the gasoline tax lien upon the property subject thereto 'shall remain until the tax is paid, or the property sold for the payment thereof.' This language was borrowed from Sec. 3716 of the Political Code of California. In 1897, before the enactment of the gasoline tax law (Cal. Stats. 1925, p. 659, sec. 4) here

involved, the Supreme Court of California had held that this language used in Sec. 3716 of the California Political Code, supra, gave a prior and paramount lien for taxes. *California Loan and Trust Co.* vs. *Weiss,* 118 Cal. 489. By the use of this language, so construed by the Supreme Court of California, in its subsequent legislation with relation to the lien of gasoline taxes, it must be held that the legislature intended the language to have the effect attributed to it by the Supreme Court in its prior opinion, hence it must be held that the tax lien for the gasoline taxes here in question was unaffected by the foreclosure and sale above mentioned."

The decision of the court below should therefore be modified so as to order that the lien of the State of California is, in any event, paramount to any antecedent contract lien which the individual claimants herein may have.

CONCLUSION

In conclusion, then, the appellant reiterates that the trial court erred in each of the foregoing particulars.

The trust deed of June 7, 1930, was, as to the property described as Parcel II, merely an attempted encumbrance of personal property, viz, of a certain leasehold interest of the El Camino Oil Company. It was not, however, executed in the manner required by law for mortgages of personal property. Said instrument was therefore invalid as against the State of California as tax creditor of

said oil company. The district court erred in ordering that the claim of said individual creditors was secured by the lien of said deed of trust as a valid lien, as against the State of California, upon said property described therein as Parcel II.

The penalties which were added to the taxes assessed upon the basis of distributions of motor vehicle fuel by the El Camino Oil Company from April 1, 1930, to June 10, 1930, inclusive, were a lien upon the property of said company. The district court properly so held, but failed to order that said lien attached as of the dates of such distributions (the same as did the lien for the taxes to which said penalties were added), and consequently *prior in time* to the recording of the chattel mortgage and deed of trust relied upon by the individual claimants. The district court erred in failing to specify in its order the date as of which said lien for said penalties attached, and in failing to order that the lien of said penalties was prior and paramount to any lien of said chattel mortgage and trust deed.

Finally, and without regard to the determination made by the court upon the foregoing propositions, the tax lien of the State of California for even that portion of its claim which accrued subsequent in point of time to the recording of said chattel mortgage and deed of trust, is paramount to even valid liens which may have been created by said contractual encumbrances. In other words, even if said deed of trust was *not invalid* as against

the State of California as to the personal property described therein as Parcel II, and even if the lien for the penalties upon the taxes based upon distributions of motor vehicle fuel from April 1, 1930, to June 10, 1930, inclusive, did *not attach* as of the dates of said distributions (the same as did the lien for the tax which was assessed upon the basis of said distributions), still, the *entire* tax lien of the State of California, is superior and paramount to even such *valid* contract liens, even though a portion of said tax lien is *subsequent in point of time* to said contract liens. The legislature of the State of California clearly expressed its intention that the lien for the taxes in question should be paramount to antecedent contract liens. There is no question as to the *power* of the legislature to so provide. It *exercised* this power by adopting language which the California Supreme Court had previously held disclosed the intention to make the tax lien paramount to antecedent contract liens. The district court erred in ordering that that portion of the State's lien which attached *subsequent* to June 10, 1930, was inferior to any lien which the individual creditors may have acquired as against the State by recording said chattel mortgage and deed of trust on that date.

The order of the district court should be modified accordingly. It should be ordered that no portion of the claim of said individual creditors is, as against the State of California, secured by said

deed of trust as upon the property described therein as Parcel II. It should be further ordered that the lien for the penalty which was added to the taxes which were based upon distributions of motor vehicle fuel from April 1, 1930, to June 10, 1930, attached as of the dates of such distributions, and so were *prior in point of time,* and so superior to any lien of the contract creditors. Finally, and ~~that~~, in any event, it should be ordered that the *entire* tax lien of the State of California is *paramount* to *any* lien of the contract creditors, even if such contract lien be earlier, in point of time, than the tax lien of the State.

Respectfully submitted.

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